DANISH MORTGAGE BANKS' FEDERATION

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Possible implementing measures under the Market Abuse Regulation

The European Securities and Markets Authority has published a Discussion Paper on the possible implementing measures under the Market Abuse Regulation.

The Danish specialised mortgage banks, represented by the Association of Danish Mortgage Banks and the Danish Mortgage Banks' Federation, welcome the opportunity to comment on the Discussion Paper. As we represent the interests of specialised covered bonds issuers in Denmark, we have focused our reply to issues related to this theme.

The difference between equity markets and bond markets

It is important that the implementation of the Market Abuse Regulation (MAR) is done in a way that prevents any form of market abuse but care must be taken that the functioning of the securities markets in the European Union is not hampered. It is important to make a clear distinction between the different markets and submarkets for securities for instance there is a big difference between the equity markets and the bond markets.

The pricing on the equity market is based on expectation to the issuing company and the industry it operates in as well as expectations on future earnings. On the bond market prices are driven by other more general factors like interest rate levels, volatility, inflation, liquidity etc. Pricing of bonds is to a much lesser extent dependent on the issuer itself than the pricing of shares. It is also important to have in mind what the driver is behind the trading in the different markets, for instance borrowers' loan related transactions in Danish mortgage covered bonds should be considered as an inherent part of the process of taking a mortgage loan, rather than a bond trade[1].

In the Danish mortgage system the bond trades that are concluded between borrowers and mortgage banks are done as an inherent part of the process of taking home or redeeming a mortgage loan. Therefore the activities of the mortgage banks must be looked at in the right context, thereby recognising that the trading activities are done as an inherent part of the primary mortgage lending business.

[1] For more information on the Danish mortgage system in the Appendix

Q39 – Cleansing strategy
We prefer option 1, as a requirement for an agreements on cleansing strategies are resource intensive and might not be needed in all cases. Option 1 gives more degrees of freedom to the disclosing participant when setting the cleansing strategy, but it does not exclude the possibility of an agreement between the parties which could be useful in some cases.

To us it is important that the regulation on cleansing strategies is easy to handle in the daily work. For instance we see no need to send cleansing information to the sounded people when a press release or market message has been sent out. This will help to reduce the costs associated with sounding and cleansing.

Q 64 - Suspicious transaction reporting
In our view, the paper does not present any valid reason for the proposal of requiring the establishing of automated surveillance systems in all firms. Hence we do not support this idea, as is would require significant investment and for many firms would not be proportionate to the risks involved.

We are of the opinion, that is should always be possible for firms to monitor order flows by using manual processes. Procedures should be based on a risk-based approach as the risk of market abuse can be very different depending on the business model of the firm and differ depending on whether the purpose of a transaction is to make an investment or the transaction is an integrated part of the process of obtaining a mortgage loan.

Q 83 - Public disclosure of inside information
According to section 307 public disclosure will always be required where the undisclosed inside information contradicts the market's current expectations. The reason being that the public otherwise would be misled.

We do not agree with this conclusion. We suggest, that only "market's current expectations" based on disclosed information by the *issuer*, should be taken into account when determining, whether disclosure is required.

Q 84 - Insider lists
We agree that the insider list must make it possible to identify the persons recorded on the list without any problems. However, we find that there is no need for the insider list itself to contain the information listed in section 318. For instance, if every employee has a unique identification number assigned to him, it will be sufficient that the firm – on request by the competent authority – is able to identify the person in question and give the authority all necessary information. Requiring that the list should hold all the information listed in section 318 would impose unnecessary burdens on the firms.

In this context it is important to bear in mind the EU Data Protection Directive. In our view the best solution would be if the implementing measures themselves consider the Data Protection Directive, instead of leaving it to the national competent authorities to make these interpretations.

Managers' transactions

Article 14 of MAR sets out a transactions notification requirement in case of managers' transactions conducted on their account relating to shares or debt instruments of the issuer in which the manager holds his position.

In match funded regimes – like the Danish mortgage market – the mortgage borrower is however not an investor but simply a borrower, and the underlying bonds are sold at market prices for mortgage loan funding purpose only. In this context the requirement in Article 14 makes no sense given the purpose of MAR, as these transactions under no circumstances will be able to have a significant effect on the price of the underlying bonds. Therefore, we are of the opinion, that the requirement in Article 14 should not apply to transactions in "own" bonds under these circumstances.

Managers' transactions in own issued covered bonds does not have nearly the same signal effect or implications on the bond prices as for instance mangers' transactions in own issued shares or corporate bonds. The notification of managers' transactions is not relevant for the marked. In the case of managers' mortgage loans these should not be considered a transaction which is part of manager's transactions in article 14 since the purpose is to take home or redeem a loan and not an investment in the debt instrument of the issuer. Hence a manager's loan transaction is of no relevance for the market.

If you have any questions in connection with our reply, please do not hesitate to contact us for further clarification.

Kind regards,

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Appendix – Danish mortgage system

The Danish mortgage system is market based and builds on the principle that the payments between borrower and the bond owners must match. The mortgage bank may only grant loans against a mortgage on real property within a fixed lending limit (loan-to-value/LTV). Therefore the mortgage bank must do a valuation of the real property, and the calculation of the loan amount must take place in compliance with a set of rules laid down by the Danish FSA. The mortgage bank also performs a credit evaluation of the borrowers.

When a homeowner is granted a loan the mortgage bank issues bonds corresponding to the contracted nominal amount, amortisation profile, interest coupon etc. The bonds are either sold in the market by the mortgage bank or transferred to the borrower who can sell the bonds in the market. If the bonds are not currently traded in the market the mortgage bank can offer to buy the bonds.

If a borrower would like to make an early repayment he can buy bonds in the market and deliver them to the mortgage bank which then cancel the bonds against the total outstanding and writes down the borrower's debt. The borrower can also ask the mortgage bank to buy the required bonds in the market or ask if they can sell the bonds from the mortgage bank's proprietary holdings. Another possibility for the borrower is in some cases to call the mortgage bond for redemption at par value.